



HOUSE BUDGET COMMITTEE

Democratic Caucus

The Honorable John M. Spratt Jr. # Ranking Democratic Member

214 O'Neill HOB # Washington, DC 20515 # 202-226-7200 #

June 20, 2001
Revised June 22, 2001

Dear Democratic Colleague:

Republicans have argued that, even after their excessive tax cut, the budget has a \$500 billion “contingency fund” to pay for further tax cuts and other Republican priorities — without invading the Medicare Trust Fund surplus. However, despite a paper reserve fund created in the budget resolution, there are virtually no resources available until 2006 at the very earliest.

The attached House Budget Committee Democratic staff analysis shows that, with the tax cut, the Republicans have already invaded the Medicare Trust Fund surplus for the near term. We improve on the Republicans’ accounting in three ways:

- We use the most up-to-date May CBO estimates. The Republicans continue to use the older March CBO estimates — because the new CBO numbers would make their projected surpluses smaller.
- We take into account the policies specified in the Republicans’ own budget resolution.
- Finally, we do not permit resources from the Medicare Hospital Insurance Trust Fund to be double-counted as also paying the cost of prescription drug coverage for the elderly.

With these improvements over the Republican accounting, and even assuming no disasters and no Bush defense buildup, the analysis shows that the Republican budget already invades the Medicare Trust Fund surplus in 2003 and 2004. The surpluses in 2005 and 2006, moreover, are extremely small. Indeed, were it not for a pure time-shift gimmick, Republicans would be spending part of the Medicare Trust Fund surplus in 2002 and 2005 (with a very small surplus in 2004) as well. Under their own budget resolution, no realistic legislation today can access the “contingency fund” that is almost exclusively in the last five years of the budget window.

Republicans, especially the majority in the House, will continue to tout their paper contingency fund with favorable budget numbers that they themselves will generate. But the fact is that Republicans are already tapping the Medicare surplus; and with each additional tax cut they pass, the amount they tap will grow.

Sincerely,

John M. Spratt, Jr.
Ranking Democratic Member



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REPUBLICAN “CONTINGENCY FUND” IS A SHELL

Republicans have argued that, even after their excessive tax cut, the budget has a \$500 billion “contingency fund” consisting of the non-Medicare, non-Social Security surplus. They assert that the Contingency Fund can be used to pay for further tax cuts and other Republican priorities — without invading the Medicare Trust Fund surplus.

The Republican budget resolution does establish a “strategic reserve fund,” and does empower the House Budget Committee chairman to “adjust the appropriate aggregates and committee allocations ... for a bill making appropriations for the Department of Defense and ... a bill providing a prescription drug benefit, and any other appropriate legislation.” This wording may provide broad latitude. But the chairman cannot allocate resources that do not exist; and there are virtually no resources until 2006 without tapping the Medicare surplus.

Republicans Have Already Invaded the Medicare Surplus

This “contingency fund” is largely a shell. With the tax cut, the Republicans have already invaded the Medicare Trust Fund surplus for the near term. Any remaining funds are available for additional tax cuts or spending only in the distant out years — when budget projections are most uncertain.

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
Contingency Fund, billions	6	25	-5	-4	1	11	21	39	73	104	206

Compared with the Republicans’ self-generated numbers, the estimates above are more accurate in three ways:

- They use the most up-to-date May CBO estimates, while the Republicans continue to use the older March CBO estimates. Republicans wrote in their report language for the budget resolution, “The Conferees agree that it would be ideal to enforce this resolution using CBO’s best cost estimates based on its most recent baseline ... This year, however, ... CBO will not release its ... revised baseline until May 18 ... Therefore the Conferees intend that the Chairmen of the Committees on the Budget will enforce this resolution ... with the assumptions underlying CBO’s revised baseline only after CBO publishes its analysis ...” The new CBO analysis has been available for a month. But **because the new CBO numbers make the projected surpluses smaller, the Republicans have not updated their estimates.** We have.

- They take into account the policies specified in the Republicans' own budget resolution. As the basis for their current estimates, the Republicans ignore the commitments that they made in their budget resolution, and consider only legislation that has already been enacted. So, for example, they pretend that they have no commitment to enact prescription drug coverage for the elderly. (We don't even include the cost of their commitments that were excluded in the budget resolution — such as the President's to-be-proposed defense buildup. Press accounts suggest that the defense program could match or exceed all non-tax commitments in the budget resolution.)
- Finally, with specific reference to prescription drug coverage for the elderly, the Republicans are now very frank that they intend to raid the Medicare Hospital Insurance Trust Fund to pay the cost. They claim that this would save money for the non-Social Security, non-Medicare surplus. True enough; but it would cut the life of the Medicare Hospital Insurance Trust Fund in half, accelerating its exhaustion by about 14 years. This Trust Fund raid would immeasurably complicate the task of reforming that program (see below).

With these improvements on the Republican accounting, the table above shows that the Republican budget already invades the Medicare Trust Fund surplus in 2003 and 2004. The surpluses in 2005 and 2006, moreover, are extremely small. Indeed, were it not for a pure timing shift gimmick, Republicans would be spending part of the Medicare Trust Fund surplus in 2002 and 2005 (with a very small surplus in 2004) as well.

Furthermore, these figures assume that everything goes according to plan — the economy follows the forecast, there are no natural disasters, and there are no changes of policy. That means that there are no additional tax cuts or spending increases of any kind — no extension of the R&D tax credit, no fix for the Alternative Minimum Tax (AMT) problem, no Bush education plan. The numbers assume that there is no increase in defense spending above the “placeholder” number in the President's budget, even though the President will increase his request as soon as the Rumsfeld review is completed. Obviously, this scenario is not credible. But even with such unrealistic assumptions, there is no meaningful contingency fund for the next several years.

The budget resolution does allow the House Budget chairman broad authority to use this “contingency fund” to increase allocations for future legislation. But the resolution proscribes that such “Legislation ... may not ... reduce the on-budget surplus below the level of the Medicare Hospital Insurance Trust Fund surplus in any fiscal year ...” — in other words, no use of the “contingency fund” by the Budget chairman may drive the non-Social Security, non-Medicare surplus below zero. And under this rule, as is clear from the table, even though it would be permissible to make an allocation from the small remaining surpluses in 2001 and 2002, that allocation may not have any budget consequences in 2003 and 2004; and no new allocation would be permissible in 2003 or 2004. There may be projected surpluses in the distant out years, but no realistic legislation today can access that far-off “contingency fund.”

Of the total “contingency fund,” 94 percent occurs only in the last five years. Of that, at least \$100 billion, in the very last year, exists only because of the additional Republican gimmick of sunsetting the entire tax cut nine months before the end of the ten-year budget window.

Republicans, especially the majority in the House, will continue to tout the favorable official

budget numbers that they themselves will generate. But Democrats should be aware that those numbers are highly questionable; and with each additional tax cut Republicans pass, the amount they divert from the Medicare surplus will grow.

A New Republican Medicare Gimmick Is Equally Ineffectual — And Disturbing

There are several other “reserve funds,” beyond the “strategic reserve fund,” in the budget resolution. All of them — except one — contain the same restrictive language prohibiting allocations that would invade the Medicare Trust Fund surplus. The one reserve fund without this restriction is the reserve fund that provides the \$300 billion allocation for prescription drug coverage for the elderly.

The absence of this restriction is yet another Republican gimmick, which was used to pretend that there is more non-Medicare surplus money to spend for even more excessive tax cuts. Here is the math: All else equal, if you pay a dollar for prescription drug coverage out of the general fund, you reduce the non-Social Security, non-Medicare surplus — the “contingency fund” — by a dollar. But if you pay that same dollar out of the Medicare Trust Fund, the non-Social Security, non-Medicare surplus — the “contingency fund” — does not change at all. (Spending the dollar from the Medicare Trust Fund reduces **both** the total surplus **and** the Medicare surplus by a dollar.) Raiding the Trust Fund makes the program seem free.

This gimmick is disturbing, for one key reason: It threatens the core Medicare program. Republicans ignore the basic fact that they can spend each dollar only once. They pretend that the dollars in the Medicare Trust Fund surplus are available to fulfill their current function — to provide hospital services to the elderly — but that they can also be used to provide a new prescription drug program. If these dollars are spent on prescription drugs, however, where will Medicare get the money to pay the elderly’s hospital bills?

In fact, if the prescription drug program costs contemplated in the budget resolution were charged to the Medicare Trust Fund, then the Medicare annual surplus would be eliminated by about 2007. Annual deficits would mushroom from that point, and the entire Trust Fund balance would likely be dissipated by about 2015 — not the 2029 date anticipated under the current law. That new exhaustion date would be just four years after the first of the baby-boom generation become eligible for Medicare. Fixing Medicare’s finances over that shorter time frame — with that much less warning time for both providers and beneficiaries — would be much more difficult.

Republicans argue that money from the Medicare Trust Fund can justifiably be used for “Medicare reform.” Providing prescription drug coverage would indeed be an important improvement to Medicare (even though Republicans now seem to welch on their commitment to drug insurance). But providing such coverage does not extend the life of the Trust Fund; and raiding the Trust Fund obviously and markedly shortens it. Perhaps the Republicans believe that, if they could so cut off the flow of money into the Trust Fund, they could hasten the day when Medicare would “wither on the vine.”

EXCESSIVE TAX CUT AND BUDGET GIMMICKS THREATEN MEDICARE AND SOCIAL SECURITY

(Billions of dollars; CBO May assumptions)

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2002-11
CONFERENCE AGREEMENT												
Baseline Unified Surplus	275	304	353	400	437	508	578	641	718	806	883	5629
Social Security	156	172	187	202	221	238	256	275	293	311	330	2487
Medicare Part A	28	38	41	43	42	45	43	42	40	36	28	397
Available Surplus	92	95	125	155	173	225	279	324	385	459	525	2745
Enacted Tax Cut	74	38	90	107	107	135	151	160	167	187	129	1272
Non-Reconciled Tax Cuts	0	3	3	2	2	3	1	1	1	1	1	20
Medicare Rx and Home Health	0	0	1	11	22	29	40	46	49	54	61	314
Other Health	0	7	13	14	6	7	6	6	6	6	6	77
Agriculture	6	7	8	8	8	7	7	6	6	7	7	74
Veterans	0	0	0	1	1	1	1	1	0	0	0	6
All Other	4	8	3	-4	-2	-4	0	-0	-0	-0	-4	-3
Resulting Net Interest	2	6	11	19	27	38	50	65	81	99	117	514
"Contingency Reserve" 1/	6	25	-5	-4	1	11	21	39	73	104	206	472
LIKELY FURTHER ACTION												
Average Historical Emergencies 2/	N.A.	2	4	5	6	6	6	6	6	7	7	55
Defense Increase 3/	0	13	21	27	32	37	45	48	49	49	49	370
IDEA 4/	0	0	6	10	13	15	18	20	21	22	23	149
AMT 5/	0	1	4	7	13	21	37	43	49	56	63	292
Resulting Net Interest	0	0	2	4	7	11	17	24	32	41	51	191
Resulting Surplus / Deficit	6	8	-40	-56	-70	-80	-102	-102	-85	-71	14	-584
Spending of Medicare Surplus	0	0	-40	-43	-42	-45	-43	-42	-40	-36	0	-331
Spending of Social Security Surplus	0	0	0	-14	-28	-35	-59	-60	-45	-34	0	-275
Memo: Funding Gimmicks 6/	-33	33		-7	7						100	
"Contingency Reserve" Without Gimmicks	39	-8	-5	3	-5	11	21	39	73	104	106	

1/ Also equal to the non-Social Security, non-Medicare surplus.

2/ Outlays resulting from House Republican estimate of historical average of \$5.6 billion per year of emergencies beginning in 2002, adjusted for inflation thereafter.

3/ Defense increase of \$250 billion in budget authority over six years to April 2001 defense plan, with increases maintained from 2008 through 2011.

4/ Outlays resulting from S. 1.

5/ Cut necessary to undo AMT effects of H.R. 3, as estimated by Joint Tax Committee.

6/ Timing shifts through corporate estimated tax payments; spurious revenue savings in 2011 because of early sunset of tax provisions.

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